

141.3

REPORT ON BUSINESS AND SERVICES
CONSOLIDATED DATA CENTER

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February 23, 1973

Honorable Willie L. Brown, Jr.
Chairman, Assembly Committee on
Ways and Means
Room 319, State Capitol
Sacramento, California 95814

Dear Willie:

Transmitted herewith is an audit report on the
Business and Services Consolidated Data Center.
This report was prepared pursuant to your recent
request.

The report discusses the progress to date on the
establishment of the first of five planned con-
solidated data centers.

Sincerely,



VINCENT THOMAS, Chairman
Joint Legislative Audit Committee

Enclosure

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SUMMARY OF FINDINGS

The findings contained in this interim report are shown below in the sequence in which they appear.

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INTRODUCTION

This is an interim report on the Business and Services Consolidated Data Center. The report covers a brief review of activities prior to July 1, 1972 as well as findings through January 26, 1973, which were observed as a result of monitoring the development of the data center.

HISTORY - PRIOR TO JULY 1, 1972

There has been considerable concern shown in past years by both the Legislature and the Executive Branch in regard to proliferation of computers and the need for consolidation. The Legislature evidenced its dissatisfaction with consolidation progress through the Budget Act of 1971. In this Act, the responsibility for statewide control and coordination of EDP was transferred from the Office of Management Services to the Department of Finance. On July 1, 1971, the EDP Control and Development Unit was established in the Department of Finance.

The State Data Processing Officer (the Chief of the EDP Control and Development Unit) and his deputy proceeded rapidly to develop a consolidation plan in order to carry out the wishes of the Executive Branch. A general plan was developed, without participation of the EDP users, and adopted by the Cabinet on April 24, 1972. The plan embodied the following:

- Five major data centers
- State teleprocessing network
- Integrated data bases (sharing common data)

- Common rates for comparable services
- Statewide standards for operating system (uniformity).

EDP Consolidation Plan Cost
Savings Cannot Be Substantiated

The EDP Control and Development Unit, in developing the EDP Consolidation Plan, arrived at an estimated savings of \$185 million (primarily cost avoidance). This was based on an assumption that a 20 percent EDP growth-rate could be projected for each of the next five years without consolidation, but with consolidation this could be reduced to a 10 percent growth-rate. Normally, a cost/benefit analysis is required to justify proposed EDP plans. The cost/benefit analysis prepared by the EDP Control and Development Unit covered only two of the five centers and did not cover all EDP costs within these two centers (e.g., systems analysts and programmers). The cost savings shown in this cost/benefit analysis was less than 10 percent of the estimated \$185 million and was not reviewed by any of the departments with EDP installations. Consolidation should produce significant savings; however, there is insufficient information available at this time to substantiate any specific savings amount.

EDP Equipment Was Procured
On a Sole Source Basis

The EDP Control and Development Unit, in proceeding to carry out the EDP Consolidation Plan, requested IBM to provide a more detailed consolidation implementation plan and determined that IBM equipment (370/165 computers) should be procured on a sole source (no bid) basis for the Business and Services Consolidated Data Center. As justification for this action, they cited the fact

that most of this center's EDP programs were compatible with IBM equipment, which would facilitate conversion and reduce total conversion costs. Also considered was the present use of an IBM 370/165 computer in the Department of Human Resources Development providing experience and backup.

The sole source contract with IBM was signed by the Department of Public Works on May 5, 1972, and later approved by the Department of Finance. The contract was for three IBM 370/165 computers and related equipment. One of these computers was to be installed temporarily in the Department of Public Works. The computer in the Department of Public Works was to be removed and returned to IBM after the other two computers were installed and operating satisfactorily at the Consolidated Data Center site, which had not been selected at that time.

Normally in the state, competitive bidding is required in order to obtain the product or service needed at the least cost to the state. Section 14807 of the Government Code requires competitive bidding but permits sole source purchases upon agreement of the Department of General Services. The contract for the three IBM 370/165 computers was for approximately \$7 million.

The sole source procurement had an adverse effect on current competition because the vendors knew of the state's original preference for IBM, the bidding process was costly for the bidders, and many of the factors that would determine who receives the contract would be determined subjectively or after the bids were opened. This contributed to the result that only two vendors submitted proposals in response to the RFP.

The Department of Public Works began installation on their site in June 1972. At that time, the site was prepared and new EDP equipment started arriving.

HISTORY - SUBSEQUENT TO JULY 1, 1972

When the Legislature became aware of the sole source procurement of EDP equipment for the Business and Services Consolidated Data Center, control language was written into Section 4 of the Budget Act of 1972 (Ch. 156; Stats. 1972). See Exhibit I (page 29). The two key features were:

- That contracts for EDP activities in excess of \$10,000 are to be competitively bid
- That contracts awarded or entered into shall be in the form of the Model Contract as outlined in Section 4960.1 of the State Administrative Manual and no portion of such contract shall be excluded or stricken.

At the same time, it was decided by the Legislature that the Department of Public Works could acquire upgraded EDP equipment. The Budget Act of 1972 then provided that the EDP equipment and related activities for the Business and Services Consolidated Data Center must be competitively bid. The contract with IBM was then revised by the Department of Public Works to reflect this decision. The contract was reduced from approximately \$7,200,000 to approximately \$1,800,000. There was also an understanding that the IBM 370/165 computer acquired for the Department of Public Works would not be used to do any work which would prejudice any bidder for the forthcoming consolidation. (The IBM 370/165 computer had the capacity to do considerably more work than was needed for the Department of Public Works.)

The Legislature enacted Chapter 787 of the Statutes of 1972 (SB 1503 - Teale) as an urgency statute, which became effective August 11, 1972. The bill

added Chapter 8 (commencing with Section 11775) to Part I of Division 3 of Title 2 of the Government Code. The chapter created four consolidated data centers, which had to be established prior to the expenditure of the funds for these centers appropriated in the Budget Act of 1972. The four centers were:

- The Law Enforcement Consolidated Data Center
- The Business and Services Consolidated Data Center
- The Revenue Consolidated Data Center
- The Human Relations Consolidated Data Center

Two sections of the Government Code added by the bill provided for on-site training, confidentiality, use of the Model Contract and competitive bidding (Secs. 11784, 11785, Gov. C.). The language in those sections was similar to that in Section 4 of the Budget Act of 1972.

The Department of Finance, in accordance with the wishes of the Legislature, as expressed in SB 1503, immediately started the competitive procurement process for the Business and Services Condoliated Data Center. The first step was the creation of an organization within the Business and Transporation Agency to carry out the procurement process and operate the up-graded computer system in the Department of Public Works. See Exhibit II (page 30) This organization had four major functions:

- "Initial conversions (Department of Public Works, Department of General Services, Office of the Secretary of State, and California Highway Patrol
- Center operations (Department of Public Works)

- Site preparation (Business and Services Consolidated Data Center)
- Procurement (Business and Services Consolidated Data Center)."

A Request for Information and Technical Capability Survey (RFI/TCS) was prepared and sent to over 800 vendors on August 14, 1972. A vendors conference to review the RFI/TCS and answer questions was held on August 29, 1972. This conference was originally scheduled to last two days, however, it only lasted 45 minutes. The procedure used by the Department of Finance was to read answers to written questions previously submitted. Additional questions were not permitted from those attending and there was no further discussion. There were 13 vendors that indicated in writing that they intended to respond to the RFI/TCS. The response received from these vendors regarding the RFI/TCS helped in clarifying certain areas when the Request for Proposal (RFP) was prepared. The RFP was released on November 6, 1972, to seven vendors:

- Allen - Babcock
- Burroughs
- Control Data Corporation (CDC)
- Honeywell
- International Business Machines (IBM)
- McDonnell - Douglas Automation Company
- UNIVAC.

Proposals, in response to the RFP, were received on January 9, 1973, from two vendors (IBM and UNIVAC) and these proposals are presently in the process of being evaluated.

During the competitive procurement process, a problem arose in regard to the reluctance of any of the major vendors to sign the Model Contract. The Legislature enacted AB 2393 (Cullen) as Chapter 1254 of the Statutes of 1972. The bill, which became effective on December 15, 1972, as an urgency statute, amended provisions of the Government Code added by SB 1503 and, in addition, required the Department of Finance to develop a revision of the Model Contract by February 15, 1972 (Sec. 3, Chapter 1254).

IMPORTANT FUTURE EVENTS

The critical future events to take place in the procurement process for the Business and Services Consolidated Data Center are:

- Benchmark tests of each vendor's equipment
 - IBM - week of January 29, 1973
 - UNIVAC - week of February 26, 1973
- Revision of the Model Contract by the Department of Finance - February 15, 1973
- Disclosure of vendor selected - March 23, 1973.

REPORT FORMAT

The remaining sections of the report are Model Contract, Business and Services Interim Data Center, and Business and Services Procurement Process. These sections cover the principal areas observed during the monitoring of the data center development. Primary findings will be presented in each of these sections with additional findings to be covered in the final report.

MODEL CONTRACT

BRIEF HISTORY

On July 1, 1972, the Budget Act of 1972, including Section 4, became operative and on August 11, 1972, the Government Code provisions added by Chapter 787 of the Statutes of 1972 (SB 1503 - Teale) became effective. The Legislature through these actions provided for control language to be used relating to the procurement of Electronic Data Processing (EDP) equipment, systems and services. Refer to Exhibits I and III (pages 29 and 31). It was apparent that the Legislature felt that some clarification of procurement guidelines was necessary because of the recent attempt at sole source procurement in the Department of Public Works.

The Model Contract, since its inception in 1967 and with a minor revision in 1969, had been used by the Department of Finance as a guideline for individual negotiation of EDP procurement contracts. In practice, each procurement established separate agreements with each vendor, all different in areas of terms and conditions.

The vendors' reaction to this control language was adverse, specifically that all EDP contracts for new equipment, systems and services be in the form of the Model Contract and no portion of such contract shall be excluded or stricken.

None of the five major vendors of main frame equipment would sign the model. It is important to note that there were major differences in the vendors' reasons for refusing to sign, as well as differing degrees of what

each would accept. Certain manufacturers of peripheral equipment did indicate that they would sign.

To resolve the problem of vendor resistance, the Department of Finance supported AB 2393 - Cullen (Ch. 1254; Stats. 1972). Essentially, the enacting of this law in December 1972, as an urgency statute, was to offer some means of modifying the restrictive language in the model, as indicated by the following:

"It is the intent of the Legislature to consider modifications to the model contract which impose conditions inconsistent with current practices in the electronic data-processing industry. Identification of such conditions by vendors shall be taken into consideration in the formulation of legislation which will relieve these difficulties in order that firms not be unreasonably precluded through the use of inappropriate contract statement from doing business with the State of California." (Sec. 11785, Gov. C. as amended by Ch. 1254, Stats. 1972, AB 2393.)

In addition, this measure allowed modification of requirements for lease of EDP equipment for specific one-time acquisitions of the State Treasurer and State Controller.

Department of Finance Approach

Section 3 of Chapter 1254 (AB 2393) stated that the Department of Finance should provide an approved revision to the Model Contract for lease of EDP systems and components, no later than February 15, 1973. The Department of Finance's approach has been to make the minimal revisions necessary in order to allow procurement for the Business and Services Consolidated Data Center. Any remaining revisions by Department of Finance are to come from a "laundry list" of topics they are preparing, to demonstrate their awareness and potential solution.

The Department of Finance has made some revisions to the original model, based on vendors' Federal G.S.A. Supply Schedules, vendor interviews, and suggestions. This revised model has been circulated to those interested vendors and their comments have been noted. Of the five major vendors, two had meetings with Department of Finance personnel; of these, one would accept and the other would not make a categorical acceptance but has reservations. The remaining three vendors were contacted by telephone; two of these had suggestions, one would accept as written, the other would not, while the third was unable to give an official response in the time available. The final comments and suggestions of all vendors are being considered by Department of Finance personnel.

Interpretation of Elective
and Discretionary Paragraphs

Perhaps the most significant issue raised in the discussions of the model was over the interpretation of format used, where paragraphs of the model were assigned a rating of mandatory, elective, or discretionary. See Exhibit IV (page 32) for particular information. The significant issue was in the elective and discretionary levels, relating to "who has the authority to elect which option should be taken, the vendor or the state representative". Department of Finance's position is that this was the vendor's option, to allow him to compete in the bidding. However, General Services Legal Counsel feels that this prerogative should be the state's. First by reason of the state's basic rights as the purchaser and second that if the vendor has the choice, this would make the very sensitive subject of competitive bidding increasingly complex to monitor and to evaluate, i.e., comparability of bids, favoritism, etc.

LEGISLATION PLANNED TO
RELAX MANDATORY REQUIREMENTS

The Department of Finance is preparing legislation which should complement and accompany the revised model. Observation in meetings and discussions with key personnel indicate that a potential area of concern will be the attempt to relax the mandatory requirements of Section 4 of the Budget Act of 1972, to allow:

- The model to be returned to the State Administrative Manual where it would be used as an administrative tool
- For contract of EDP services to be on a separate contract from the model
- An attempt to reduce the restrictions inherent in the complex structure of competitive bidding.

Until new legislation is enacted, Section 4 and Section 11775, and following, of the Government Code provide control language for EDP procurement and activities. Any new legislation should be reviewed in respect to its impact on these control features.

To prevent legislation problems relating to the Model Contract in the future, the Department of Finance has mentioned that an annual review of the model will be made (to keep up-to-date with industry practices and state standards) with an annual report to the Legislature of action taken. An annual review of this nature would be beneficial to the state.

The Department of Finance is planning on using two different contracts (one for equipment based on the Model Contract, the second for related services based on sources other than the Model Contract) in the Business and Services Consolidated Data Center procurement. This position does not appear to be in accordance with the Legislature's intent, as expressed in Section 4 and Section 11785 of the Government Code. Also see Legislative Counsel's opinion number 18166. Refer to Exhibit V (page 33), which states that all contracts for EDP activities are required to be in the form of the Model Contract. The revised Model Contract to be prepared by the Department of Finance by February 15, 1973, would only cover the leasing of hardware and would not cover software of services.

LEGISLATIVE CONTROLS
NOT PROVIDED FOR AT THIS TIME

As previously explained, the Department of Finance is using a minimal approach in the preparation of a revised Model Contract and related legislation. This approach leaves a number of issues still unresolved. These issues are:

- Contract services - Typically, the cost of conversion is a significant factor in any evaluation; and, in the case of the Business and Services Consolidated Data Center, the cost exceeds \$5 million from either vendor. The Department of Finance's position is that the services area is not to be included in the model.
- Specialized contracts for EDP activities will be required, in addition to the revised Model Contract but are not currently planned; such as,

- Purchase of EDP equipment
- Purchase or lease of software.
- Competitive bidding process - Removed from Section 11785 of the Government Code (as added by SB 1503) by the amendment of that section by AB 2393. Therefore, competitive bidding is applicable only to EDP activities financed by funds subject to Section 4 of the Budget Act of 1972 and will be applicable only so long as those funds are encumberable. (June 30, 1973)
- Contractor training on site -
 - Strict interpretation would create massive problems (cost and logistics) for the state and the contractor.
 - A liberal interpretation for compliance would allow exceptions when compliance is not practicable.
 - The Legislative Counsel's opinion number 18166, states that the vendor may not perform training off of the state premises. (EDP installation) See Exhibit V (page 33).

DEPARTMENT OF FINANCE
PLANS TO CHANGE SECTION 4 LANGUAGE

It was observed that the Department of Finance intends to have Section 4 in the Budget Act of 1973-74 different from the Section 4 in the Budget Act of 1972-73. We understand the controls for competitive bidding and the use of the Model Contract are to be changed. If the control language of this section is changed, then this would have major impact on the Model Contract issue.

The Budget Act of 1973-74 has been introduced (SB 80, AB 110).
The control language for competitive bidding has been changed to "secured on a competitive basis", and the reference to contracts being in the form of the Model Contract has been eliminated.

BUSINESS AND SERVICES INTERIM
DATA CENTER

The "Interim Data Center" is a title the Executive Branch has used to describe the upgraded computer installation at the Department of Public Works. This center was planned by the Department of Finance to be used in certain conversion efforts, which would assist the development of the Business and Services Consolidated Data Center. Hereafter, when "Interim Data Center" is used it refers to the upgraded computer installation in the Department of Public Works.

The "Interim Data Center" was initiated on July 1, 1972, and is expected to remain in existence until the transfer of operations to the final site at the Department of Motor Vehicles. The Legislature has specifically authorized the upgraded computer installation at the Department of Public Works. However, there was an understanding that this system (IBM 370/165) would not be used to do any work which would prejudice any bidder for the forthcoming consolidation.

The findings related to the interim center are covered in this section.

PLANNED OVEREXPENDITURE OF ITEM 61.3

Item 61.3 of the Budget Act of 1972, appropriated \$100,000 to pay "for shipping and installation costs related to the rental of a computer, Department of Public Works, exempt from Section 4 of this act". We understand that the Executive Branch subsequently interpreted Item 61.3 to include

increased equipment costs for the IBM 370/165 computer, but not to exceed \$192,000 (appropriation of \$100,000 plus reimbursements of \$92,000).

The Department of Public Works (during fiscal year 1972-73) has incurred expenses totaling \$383,000, including the purchase of a motor generator, rental of proprietary software packages, rental of memory devices and terminals, personnel costs and increased equipment cost of the IBM 370/165 computer over the previous 360/65 computer. The Business and Services Agency has directed the data center to reimburse the Department of Public Works for these charges and to use funds from Item 61.3. Since August 31, 1972, only \$3,150 for freight costs has been charged to Item 61.3.

The effect of this action would be that an amount of \$283,000, in excess of the original appropriation would be charged to this item, the excess to be funded from reimbursements. If this is consummated, then this additional expense is assumed by the Business and Services Agency to be exempt from Section 4 of the Budget Act of 1972, specifically the requirements for competitive bidding and contract conformance to the Model Contract. This additional amount was not approved by the Legislature.

It is apparent from the above that there is a plan to use Item 61.3 for expenditures not originally intended.

IMPROPER PROCUREMENT
OF THE MOTOR GENERATOR

The Department of Public Works procured a motor generator for the "Interim Data Center" at a cost of \$15,000. The procurement of this equipment was necessary for the IBM 370/165 computer to prevent the loss of data in the event of a power failure.

Traditionally, this type of procurement is processed through the Department of General Services with competitive bidding and approval by the proper authorities. This procurement was an exception to that rule. The generator was supplied to the job site by IBM and installed by the electrical contractor.

An investigation revealed that at the time the generator was delivered there was no authorization or typical procurement paperwork prepared. This procurement was completed on a sole source basis, without competitive bidding or authorization by proper authority to forego competitive bidding. The generator is manufactured by General Electric and sells for \$13,700. The Department of Public Works now wants to charge the cost of procurement to Item 61.3, which did not exist at the time of selection and installation.

In summary, the motor generator was procured by a method outside of the established state procurement system and on a sole source basis without any approval or authorization; the Department of Public Works paid a premium price to IBM, while the manufacturer, General Electric, sold the model off the shelf for \$1,300 less; and the Department of Public Works wants to charge this expense to Item 61.3. As of the date of this report, approximately seven months later, the proper paperwork has not been authorized.

IMPROPER CHARGING OF
"INTERIM CENTER" SITE COSTS

The preparation of the site for the "Interim Data Center" started in June 1972 and was completed in July 1972. The cost of the site preparation was \$65,000.

Typically, the charge for this cost would have been made to the Department of Public Works since all other "Interim Data Center" charges are made to this department. Item 61.3 of the Budget Act of 1972 was established to provide funds for freight and installation costs of the "Interim Data Center". Site preparation costs are a normal installation cost. It appears that Item 61.3 should be charged.

The Department of General Services' Architecture Revolving Fund was charged for the site preparation cost. We understand this action was directed by the Department of Finance, and the Department of General Services will not be reimbursed. There is no apparent justification for this action.

IBM PROPRIETARY SOFTWARE
(CICS) HAS NOT PERFORMED SATISFACTORILY

The "Interim Data Center" management in July 1972, procured a proprietary software package called CICS from IBM. This package has not worked satisfactorily to date, however, IBM is attempting to take corrective action. Normally, proprietary software programs written for a specific system are usable when delivered.

The problems with CICS have forced the state to continue using a current package (called FASTER) which does not offer the features purportedly provided by CICS. The state is paying \$750.00 per month for CICS and the package is not functional.

The "Interim Data Center" management authorized the procurement of the CICS package without fully investigating its functional reliability in the centers' environment.

"INTERIM DATA CENTER" EDP
EQUIPMENT IS MEETING PERFORMANCE STANDARDS

The IBM 370/165 system hardware performance meets or exceeds established standards of reliability. The "Interim Data Center" equipment is operating at a reliability rate in excess of 95 percent.

The IBM equipment in the "Interim Data Center" is performing adequately at the present time although performance in the months immediately after installation (July - November 1972) was below expectation.

BUSINESS AND SERVICES PROCUREMENT PROCESS

The monitoring of the procurement process for the Business and Services Consolidated Data Center included the areas of the Request for Information and Technical Capability Survey (RFI/TCS), the vendors initial conference, preparation and writing of the RFP, the organization established for the procurement process, the plans for evaluation of proposals and the evaluation and selection of vendors.

The findings related to the procurement process are covered in this section.

IBM HAS COMPETITIVE ADVANTAGE DUE TO THE INTERIM DATA CENTER AND THE STATE'S USE OF STRUCTURALLY SIMILAR EQUIPMENT

Several factors have combined to provide the IBM Company with a significant advantage in the competition for the Business and Services Consolidated Data Center procurement.

First and foremost was the installation of the IBM 370/165 computer in the Department of Public Works. Subsequently, this installation was called the "Interim Data Center" by the Executive Branch and involved the conversion of programs of the Department of Public Works, General Services Center II, Office of the Secretary of State and the Highway Patrol to the new equipment. A total of 3,800 programs were converted to the new equipment by state personnel. UNIVAC estimates their cost of converting these programs to the UNIVAC 1110 to be \$1,143,200. In addition, the state cost to support UNIVAC's conversion of these 3,800 programs has been estimated by the Department of Finance to be in

the area of \$1.5 million. Therefore, the combined advantage to IBM as related to its bid for the proposed Business and Services Consolidated Data Center is estimated to be a minimum of \$2.9 million.

Secondly, the procurement of proprietary software for use on the "Interim Data Center's" IBM 370/165 computer has provided at least a \$50,000 advantage to IBM in that UNIVAC must provide comparable items of software as part of their total bid price.

Third, IBM has an advantage over the competition because of the similarity in architecture between the proposed IBM 370/165 computer and the IBM 360 and RCA Spectra 70 equipment being replaced. Approximately two-thirds of the 6,500 programs to be converted are currently on equipment structurally compatible to IBM.

IBM is faced with a relatively easy conversion of those installations now using either IBM 360 or RCA equipment, whereas, UNIVAC has no inherent advantage because their equipment is not similar to anything presently in use within the state. In installations such as Water Resources and State Teachers' Retirement System, both vendors face a problem of equal complexity because the equipment currently in use (Control Data and Honeywell) is dissimilar with either system being proposed as a replacement. In the Department of Motor Vehicles, IBM has a tremendous advantage because of the structural compatibility between the IBM 370/165 computer and the existing RCA Spectra 70's. In the balance of the installations being converted, IBM also has a decided advantage.

In summary, it appears that the "Interim Data Center" has provided IBM with a significant competitive advantage. This advantage could be reduced considerably if the conversion efforts in the "Interim Data Center" were

compensated for during the cost adjustment process to be performed by the Evaluation and Selection Committee.

NO PROVISION FOR ADJUSTING
STATE COST IN EVALUATION PLAN

Traditionally, a bid evaluation plan is required to be prepared before the opening of the proposals, so that the evaluating criteria are as objective as possible and are not influenced by the content of the proposals.

Without having a prescribed procedure for adjusting state costs before opening the proposals, it is possible to favor one or the other vendor by the methods of adjusting costs.

The evaluation committee did not include guidelines for determining adjustments to state costs. This is a difficult task, because all situations would have to be considered. However, it is necessary to at least provide guidelines to insure that the evaluation is not influenced by personal opinion after the proposals are opened and to promote evaluation on an objective basis.

COST AJUSTMENT FACTORS
COULD DETERMINE SUCCESSFUL BIDDER

The Department of Finance proposes to use "bid cost adjustment factors" to reflect the state's cost to support each vendor in such areas as conversion, training, program management, etc. Additional bid cost adjustment factors are anticipated to reflect additional costs in equipment, software, training, etc., where the vendor is felt by the state to be deficient.

These factors may very easily amount to many millions of dollars and could serve to make the low bidder appear the most costly. The use of any

such factors must be carefully monitored, fully substantiated, and well documented because their indiscriminate usage could precipitate a protest, court suit, bad publicity and above all could further deteriorate the spirit of competitive bidding between equipment vendors and the Department of Finance.

RECOMMENDATION

- A special task force should be created to carefully evaluate the bid cost adjustment factors appropriateness before the successful vendor is selected.

FAILURE OF BOTH BIDDERS TO MEET MANDATORIES

A basic consideration in the RFP was for each vendor to comply with specific mandatory requirements. Mandatory items defined in the RFP are those "which must be met in order that the proposal may be deemed responsive to the state's needs. The bid must be deemed non-responsive if the stated requirement is not met. The mandatory items may be waived by the state if the deviation is not material. A material deviation is defined as a deviation which has a potential effect on quantity, quality, price or delivery."

A vendor may be excluded from further consideration fairly or unfairly, based on how the mandates are waived or not waived. This adds increased emphasis to the vendor's effort to meet all mandates.

The evaluation process has come to a point where a determination has been made, that each of the two vendors responding has failed some mandates. One vendor failed 11 mandatory requirements and the other failed 18.

The evaluation and selection team, under the direction of the Department of Finance, is determining the materiality of those mandates that have not been met. We understand, that if those mandates which are unmet can be met by some adjustment of cost, they will be adjusted. If not, then the vendor in question will be told that he has failed to respond to necessary qualifications in the RFP and will be excluded from further competition.

RECOMMENDATION

- Require an independent review of the determination made regarding each vendor meeting the RFP mandatory requirements and the extent of any related cost adjustment.

CONTRACT TERMS AND CONDITIONS UNKNOWN TO BIDDERS

Only two vendors of EDP equipment have responded to the RFP and they are completing the procurement process without knowledge of the final contract terms and conditions.

The Department of Finance realized early in the procurement the effect that Section 4 of the Budget Act of 1972, and the statutory language added by SB 1503 would have on the vendors. In an attempt to resolve the problems created by this control language and yet to achieve the procurement in an expedient fashion, the Department of Finance supported AB 2393. They also provided in the RFP flexibility to the vendors through conditional comments in the area of the Model Contract. The conditional language in the RFP is as follows:

"Proposals received which evidence a deviation from the current Model Contract will be considered conditional, until such time as new contract legislation is enacted.

When new legislation is enacted (or, if introduced, fails to be enacted), vendors submitting proposals will be given approximately two weeks to confirm or modify their cost schedules in response to the then current contract requirements."

The two vendors who have responded to the RFP with proposals have each invested hundreds of thousands of dollars in preparing their proposals and in the benchmarks. The state, as well, has invested considerable amounts of time and money. This effort is proceeding to a day when an unknown contract will be developed to which the vendor must conform. The effect of the new Model Contract when available would be impossible to predict. However, each vendor is aware that the new model may require price adjustments or other action. The vendors' actions should be of major concern to the state, because they are not predictable. Contingency plans might be considered and alternatives reviewed.

All of the vendors participating in the RFP process have voiced their concern over the less-than-stable position of the Model Contract and that it would be a significant factor in their consideration to bid.

MATERIAL IN APPENDIX A OF THE
RFP WAS PREPARED BY ONE OF THE VENDORS

The material for Appendix A (Consolidation Implementation Management and Conversion Approach) of the RFP was prepared by IBM. This material was prepared at the request of the Department of Finance as a proposed preliminary implementation approach for EDP consolidation. This approach was then adopted by the Department of Finance and the Consolidated Project Office (CPO) for

the state and included in the RFP so that it would be available to all competing vendors and provide each with equal knowledge.

An RFP is typically written in its entirety by state personnel (or by a non bidder) and submitted at the same time to all vendors who might bid. This is done to prevent any unfair advantage being gained by any of the bidders.

By preparing a portion of the RFP to which he will later respond provides the vendor with an opportunity to present his concept and approach, which could be unique, and requires the other competing vendors to comply. It also provides the vendor who wrote the material an advantage in that he knows of the material at an earlier date and is more familiar with it.

SITE PREPARED BASED ON
MAXIMUM VENDOR REQUIREMENTS

A contract has been awarded for preparation of the site for the Business and Services Consolidated Data Center. Maximum electrical and cooling requirements of all seven potential vendors were provided for in preparing the site before the vendor was selected.

Usually, the EDP equipment is selected before the site is prepared to avoid any unnecessary expenses. The Consolidated Project Office (CPO) and the Department of Finance made the decision to proceed before selecting the EDP equipment vendor in order to expedite installation and obtain purported equipment and personnel savings at an earlier date. This approach does provide the vendor who has the maximum site requirements (IBM) an advantage, since his extra site costs will already be absorbed by the state (e.g., chilled water, extra conduit for motor generators, etc.).

The extra site costs for IBM have not been determined. These costs should be determined and considered when evaluating the vendors' proposals and making cost adjustments.

It is interesting to note that the original estimate of the Office of Architecture and Construction for the site preparation costs was \$912,000. The competitive bids received ranged from \$578,600 to \$632,469. The low bidder at \$578,600 was awarded the contract, which was approximately 63.4 percent of the original estimate.

INITIAL VENDOR ADVANTAGE
IN SUBSEQUENT DATA CENTERS

The Business and Services Consolidated Data Center is the first of four consolidated centers and the largest. The selection of the vendor to supply the equipment for this data center will have a significant effect on the selection of equipment for future data centers.

In subsequent consolidated data center procurements, each vendor will be evaluated as to his ability to meet the requirements of the RFP. The impact of a large on-going system, however, would be of ever increasing significance in the evaluation process. The vendor selected for the first center would have an advantage in the competition for providing equipment to subsequent centers. Once a major conversion commitment has been made, the vested costs to the state are substantial.

Some of the benefits to the state accruing from selecting the same vendor for each consolidated data center are:

- Equipment backup
- Ease of training
- Ability to exchange data or to communicate between systems
- Fewer operating system and software packages to maintain
- Familiarity with system and the ability to interchange personnel.



Walter J. Quinn
Acting Deputy Auditor General

February 15, 1973

Staff:

Michelmores
Hainline
Ross

Section 4, Budget Act 1972-73

GENERAL SECTIONS

SEC. 4. Notwithstanding any other provisions of this act, no appropriations made herein, or funds obtained from any other source, other than \$10,000 may be expended by any state entity for any single expansion, improvement or addition to electronic data-processing activities, personnel, equipment, facilities or supplies during fiscal year 1972-73, or any expenditure budgeted for fiscal year 1973-74 for electronic data-processing activities, personnel, equipment, facilities or supplies unless the Department Director certifies (or in the case of a consolidated data center, the center director), and the Director of Finance determines and states in writing that the criteria and procedures set forth in the Supplementary Report of the Committee on Conference on the Budget Act of 1972 have been met and followed.

Notwithstanding any other provisions of this act, no appropriations made herein, or funds obtained from any other source, may be expended by any state entity pursuant to a contract for expansion, improvement or addition to electronic data-processing activities, personnel, equipment, facilities or supplies as defined in the Supplementary Report of the Committee on Conference on the Budget Act of 1972, during fiscal year 1972-73 or any expenditure budgeted for fiscal year 1973-74 for such activities in excess of \$10,000, unless the contract for the acquisition or rental of equipment, personnel, or supplies as these terms are defined in the Supplementary Report of the Committee on Conference on the Budget Act of 1972 is competitively bid.

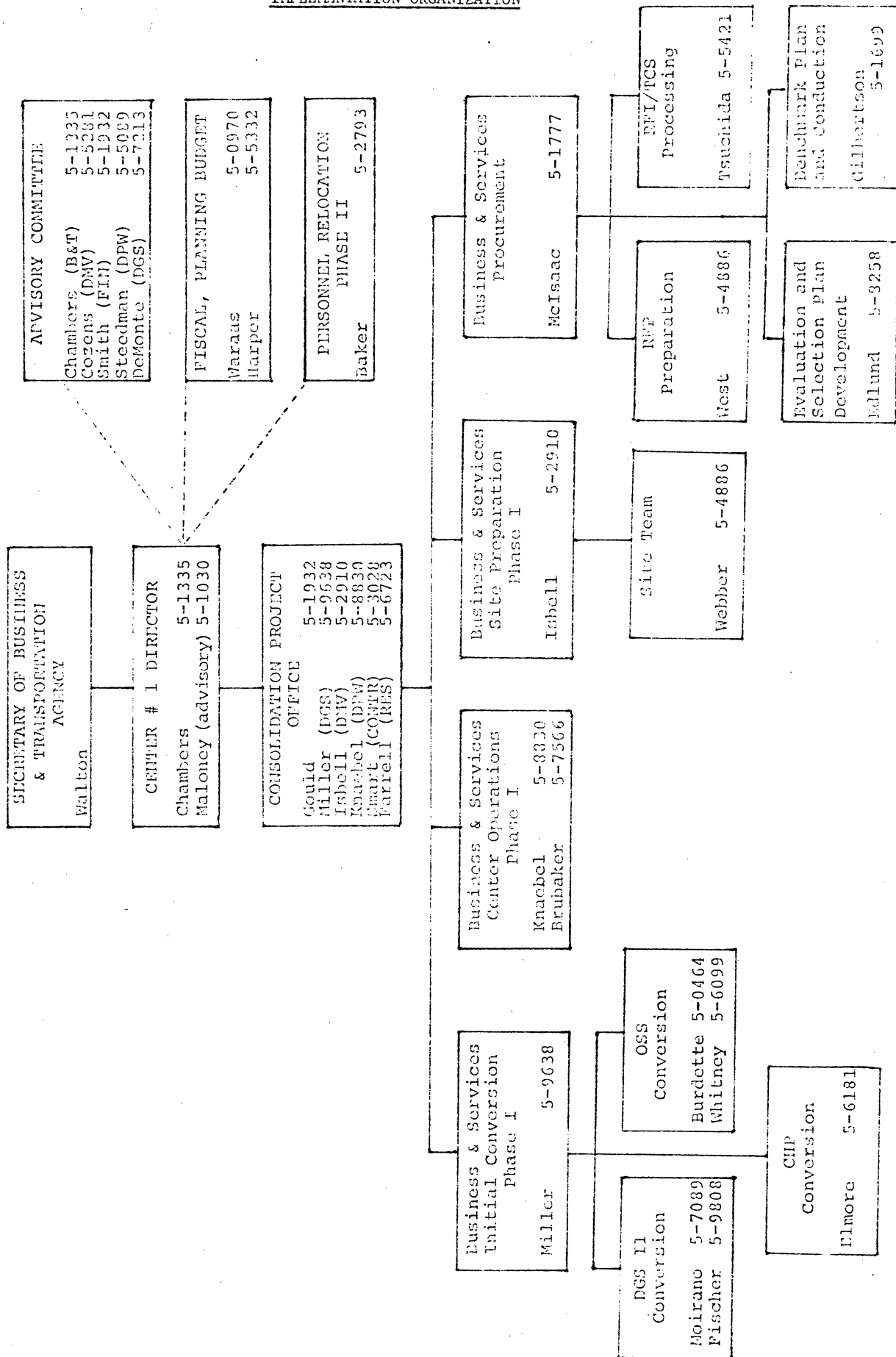
No expenditure of funds for data-processing activities shall be authorized until the director of the department requesting the expenditure and the Director of Finance certify that adequate safeguards have been developed following the criteria contained in the Supplementary Report of the Committee on Conference on the Budget Act of 1972 to insure the confidentiality of data.

The provisions of this section shall not apply to the University of California, the State Compensation Insurance Fund, or agencies provided for by Article VI of the Constitution or the Legislature.

Contracts awarded or entered into pursuant to this section shall be in the form of the model contract for lease and/or purchase of electronic data-processing systems and computers as outlined in Section 49601 of the State Administrative Manual revised new January, 1967, and no portion of such contract shall be excluded or stricken.

**BUSINESS AND SERVICES
CONSOLIDATED DATA CENTER
IMPLEMENTATION ORGANIZATION**

EXHIBIT II



Excerpt from SB 1503

11784. Any contract entered into by the Department of Finance, any state agency, or any consolidated data center, concerning data-processing systems design, programming, documentation, *conversion*, training, and other aspects of data-processing operations shall require that contract personnel shall be physically on the premises of the consolidated data center or state entity in the conduct of systems design, programming, documentation, and training and such contract shall also contain a provision requiring the contractor and all of his staff working under such contract to maintain all information obtained as a result of such contract as confidential and to not divulge such information to any other person or entity. Where contracts are entered into pursuant to this section, as a condition of such contract, provision shall be made that state personnel are to be working directly with such contract personnel to assure continuation of all projects for which the contract is let after a contractor has fulfilled his contractual obligations. *Full documentation of all programs shall reside both in the data center and the state entity for which the program was written.*

11785. Contracts awarded or entered into pursuant to this chapter shall be in the form of the model contract for lease and or purchase of electronic data-processing systems and computers as outlined in Section 4950.1 of the State Administrative Manual revised new January, 1967, and no portion of such contract shall be excluded or stricken.

All such contracts entered into pursuant to this section, where the total annual amount exceeds ten thousand dollars (\$10,000), shall be subject to competitive competitively bid.

Introduction to Model Contract

Model Form

(Rev: 12-27-72)

The following text is a model for use in leasing computer system equipment. The format (general scope and sequence of paragraphs) is mandatory; no numbered paragraph may be deleted or stricken. Appropriate entries will be made in blank spaces (indicated as "_____").

Three categories of discretion are provided: mandatory, elective, and discretionary, as further defined below. Mandatory paragraphs or subparagraphs are indicated by [M]; no changes will be permitted to paragraphs so identified. Subparagraphs identified by [E] are elective (a choice of language is provided); no changes will be permitted to the subparagraph selected. Paragraphs and subparagraphs identified by [D] are discretionary, and are offered as guidance because of the impracticality of providing exact language to be used verbatim in a specific situation. Changes to items identified [D] are subject to specific approval by the Department of Finance and General Services.

The following text will be included on the face of the State's Standard Agreement, Form 2:

[M] Contractor agrees to furnish and install at a site designated by the State in the vicinity of _____ and to let to the State, and the State hereby hires from the Contractor all those electronic data processing machines and special features and accessories listed on attached Rider B. The following Riders and Addendum are hereby incorporated by reference and made a part hereof:

Rider A. Terms and Conditions Applicable to Rental of Electronic Data Processing Systems and Components

Rider B. Equipment List, Prices, Installation Dates, and Option

Rider C. Programming Aid List

Rider D. Additional Contractor Commitments

Fair Employment Practices Addendum, Form 3

Additional Riders and/or addendums, if appropriate, will also be listed.

The text for Rider A follows:

Rider A. Terms and Conditions Applicable to Rental of Electronic Data Processing Systems and Components

[H] 1. Definition of Terms

- a. DATA PROCESSING SYSTEM - The total complement of Contractor-furnished individual machines or components which are acquired to operate as an integrated group, and are interconnected entirely by the Contractor's power and/or signal cables.

BERNAR CZESLA
CHIEF DEPUTY

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OWEN K. KUNS
RAY H. WHITAKER

KENT L. DECHAMBEAU
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DEPUTIES

Honorable Willie L. Brown, Jr.,
319 State Capitol

Electronic Data Processing - #18166

Dear Mr. Brown:

QUESTION NO. 1

Do Section 4 of the Budget Act of 1972 (Stats. 1972; Ch. 156) and Senate Bill No. 1503 (Ch. 787; Stats. 1972) require contracts for data processing services to be in the form of the model contract for lease and/or purchase of electronic data processing systems and computers as outlined in Section 4960.1 of the State Administrative Manual revised new January, 1967?

We are asked to assume the data processing services to be contracted for are as defined in Vol. 1 of the Request for Proposal for the Business and Services Consolidated Data Center, that is to say a contract for project management, training, and conversion. As we understand it, the contract for services is to be completely divorced from any hardware, i.e., is to be for services alone.

OPINION NO. 1

We are of the opinion such contracts are required to be in the form of the model contract.

ANALYSIS NO. 1

Section 4 of the Budget Act of 1972 (Stats. 1972, Ch. 156)¹ imposes certain limitations and requirements upon the expenditure of funds for data processing. Section 4 provides as follows:

"Sec. 4. Notwithstanding any other provisions of this act, no appropriations made herein, or funds obtained from any other source, over \$10,000 may be expended by any state entity for any single expansion, improvement or addition to electronic data-processing activities, personnel, equipment, facilities or supplies during fiscal year 1972-73, or any expenditure budgeted for fiscal year 1973-74 for electronic data-processing activities, personnel, equipment, facilities or supplies unless the Department Director certifies (or in the case of a consolidated data center, the center director), and the Director of Finance determines and states in writing that the criteria and procedures set forth in the Supplementary Report of the Committee on Conference on the Budget Act of 1972 have been met and followed.

"Notwithstanding any other provisions of this act, no appropriations made herein, or funds obtained from any other source, may be expended by any state entity pursuant to a contract for expansion, improvement or addition to electronic data-processing activities, personnel, equipment, facilities or supplies as defined in the Supplementary Report of the Committee on Conference on the Budget Act of 1972, during fiscal year 1972-73 or any expenditure budgeted for fiscal year 1973-74 for such activities in

¹ Hereafter Section 4.

excess of \$10,000, unless the contract for the acquisition or rental of equipment, personal services, or supplies as these terms are defined in the Supplementary Report of the Committee on Conference on the Budget Act of 1972 is competitively bid.

"No expenditure of funds for data-processing activities shall be authorized until the director of the department requesting the expenditure and the Director of Finance certify that adequate safeguards have been developed following the criteria contained in the Supplementary Report of the Committee on Conference on the Budget Act of 1972 to insure the confidentiality of data.

"The provisions of this section shall not apply to the University of California, the State Compensation Insurance Fund, or agencies provided for by Article VI of the Constitution or the Legislature.

"Contracts awarded or entered into pursuant to this section shall be in the form of the model contract for lease and/or purchase of electronic data-processing systems and computers as outlined in Section 4960.1 of the State Administrative Manual revised new January, 1967, and no portion of such contract shall be excluded or stricken." (Emphasis supplied.)

Senate Bill No. 1503 (Ch. 787; Stats. 1972²), added Chapter 3 (commencing with Section 11775) to Part 1 of Division 3 of Title 2 of the Government Code, creating four consolidated data centers for the performance of certain data processing functions. The parts of the bill relevant to the question at hand are Sections 11784 and 11785 of the Government Code,³ which provide as follows:

² Hereafter S.B. 1503.

³ Both these sections were amended by A. B. 2393 currently before the Governor. For the purposes of our discussion the amendments are not relevant. They, in fact, allow modifications of the model contract for two specific contracts for a limited period of time.

"11784. Any contract entered into by the Department of Finance, any state agency, or any consolidated data center, concerning data-processing systems design, programming, documentation, conversion, training, and other aspects of data-processing operations shall require that contract personnel shall be physically on the premises of the consolidated data center or state entity in the conduct of systems design, programming, documentation, and training and such contract shall also contain a provision requiring the contractor and all of his staff working under such contract to maintain all information obtained as a result of such contract as confidential and to not divulge such information to any other person or entity. Where contracts are entered into pursuant to this section, as a condition of such contract, provision shall be made that state personnel are to be working directly with such contract personnel to assure continuation of all projects for which the contract is let after a contractor has fulfilled his contractual obligations. Full documentation of all programs shall reside both in the data center and the state entity for which the program was written.

"11785. Contracts awarded or entered into pursuant to this chapter shall be in the form of the model contract for lease and/or purchase of electronic data-processing systems and computers as outlined in Section 4960.1 of the State Administrative Manual revised new January, 1967, and no portion of such contract shall be excluded or stricken.

"All such contracts entered into pursuant to this section, where the total annual amount exceeds ten thousand dollars (\$10,000), shall be competitively bid." (Emphasis furnished.)

As can be seen from both Section 4 and Section 11785, contracts subject to the section and the chapter are to be in the form of the model contract.

Contracts for services are specifically subject to Section 4 (emphasized portion of Sec. 4; see also, Supplementary Report of the Committee on Conference Relating to the Budget Bill of 1972, p. 16). Similarly, contracts necessarily for services by their nature are subject to Section 11735 (emphasized portion of Sec. 11734). It is apparent that contracts for services are, as a result, subject to the provisions of Section 4 and S. B. 1503. By the literal terms of the sections such contracts are required to be in the form of the model contract. We accordingly, so conclude.

In reaching this conclusion we have considered the fact the model contract is entitled a "model contract for lease of electronic data-processing systems and components" and the fact the model contract does not readily lend itself to a contract for services only as it is oriented in the main to contracts for hardware.

We anticipate, in view of that fact, that in the circumstances where a contract for EDP services only is to be entered into there will be provisions of the model contract form that are clearly not applicable (i.e., dates for delivery and installation of equipment (see Paragraph 3, Model Contract for lease of Electronic Data Processing Systems and Components, Sec. 4960.1, State Administrative Manual)). We think that the inclusion of such terms in a contract for services only, along with an appropriate designation that such clause or provision is not applicable because the contract is for services only, complies with the apparent legislative intent in requiring all EDP contracts to be in the form of the model contract, without excluding or striking any provision. Stated differently we are of the opinion that, in view of the specific requirement the model contract be used for services, the fact it would be difficult to use does not preclude such use and the fact a provision of the model contract is marked not applicable does not mean it is excluded or stricken.

QUESTION NO. 2

May a vendor on an electronic data processing contract subject to Section 4 or S. B. 1503, do training of state employees off state premises?

OPINION NO. 2

We are of the opinion a vendor may not perform training off the premises.

ANALYSIS NO. 2

By the terms of Section 4 of the Budget Act, no funds may be paid on any data processing activities unless the terms of the Supplementary Report of the Committee on Conference on the Budget Act of 1972 have been met and followed. That report, on page 25, requires as follows:

"C. Any contract entered into by the Department of Finance or other state entity shall provide for the contracting staff to be physically on the premises of the data center of state entity performing systems, design, programming, documentation, conversion, training and all other aspects for which the contractor is hired under contract. Where contractors are hired under the above conditions to perform or assist in the performance of EDP systems design, programming, implementation and documentation, state personnel are to be working directly with such contracted personnel to assure continuation of all projects after contractor has fulfilled his contractual obligations." (Emphasis added.)

Similarly, S. B. 1503 provided the same thing in Section 11784 as set forth in Analysis No. 1.


Accordingly, we conclude that the training must be on the premises.

In reaching this conclusion, we recognize the model contract to which such contracts are required to conform, provides in Section 13(a) thereof (4960.1 State Administrative Manual, Sec. 13(a)) that training may be conducted at contractor's training location.

We are of the opinion, however, that to the extent the model contract and the specific language of both Section 4 of the Budget Act and Section 11784 of the Government Code are in conflict, the statutory provisions will prevail.

Very truly yours,

George H. Murphy
Legislative Counsel


Jerry L. Bassett
Deputy Legislative Counsel